STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Apple Canyon Utility Company	:	
	:	
Proposed general increase in Water Rates.	:	09-0548
	:	
	:	(Cons.)
	:	
Lake Wildwood Utilities Corporation	:	09-0549
	:	
Proposed general increase in Water Rates.	:	

REPLY BRIEF OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION

June 25, 2010

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NOW COME the Staff witnesses of the Illinois Commerce Commission ("Staff"), by and through their undersigned counsel, pursuant to Section 200.800 of the Illinois Commerce Commission's Rules of Practice (83 Ill. Adm. Code 200.800), and respectfully submit their Reply Brief in the instant proceeding.

I. INTRODUCTION

Initial Briefs ("IB") were filed on June 15, 2010, by Apple Canyon Utility Company ("ACUC") and Lake Wildwood Utilities Corporation ("LWUC") ("Co. IB") and the Apple Canyon Lake Property Owners Association and Lake Wildwood Association, Inc (collectively "Intervenors") and Staff. Staff's Initial Brief identified and responded to many if not most of the arguments raised in the Companies' and Intervenors' Initial Briefs. In this Reply Brief, Staff has incorporated many of those responses by reference or citation to Staff's Initial Brief. However, in the interest of brevity, Staff has not raised and repeated every argument and response previously addressed in Staff's Initial Brief. Thus, the omission of a response to an argument that Staff previously addressed simply

means that Staff stands on the position taken in Staff's Initial Brief because further or additional comment is neither needed nor warranted.

II. RATE BASE

A. Intervenor's Adjustment for the Billing System

The Intervenors proposal to disallow the cost for the billing and accounting systems because the amount included in rates for the customers of LWA and ACLPU should not exceed the nationwide average of $1.50 per customer per month asserted by Company witness Lubertozzi (LWA/ACLPOA IB, p, 21, citing Tr., at 120), should be disregarded. The Intervenors supported their proposal by attempting to calculate the allocated cost of the billing and accounting systems on a per customer basis. (LWA/ACLPOA IB, pp. 21-23) Although the calculation of the revenue impact on a customer's bill cites to information located in the record from the testimony of the Companies and Staff, it does not consider all the necessarily related items in the revenue requirement. As such, the calculation is flawed.

The proposal to disallow the cost for the billing and accounting systems is apparently the result of the Company's testimony during cross examination regarding the nationwide average cost of the systems per customer. However, the statement that the nationwide average cost per customer is $1.50 has not been substantiated with workpapers. The record does not include the basis of the calculation. It is too late in the proceeding to conduct discovery so as to get the basis of the calculation into the record. A comparative analysis cannot be conducted without knowing the basis of the calculation.

However, it appears that the Intervenors' calculation lacks several elements that are essential in the calculation of any revenue requirement, e.g. accumulated depreciation, accumulated deferred income taxes, and interest synchronization adjustment. The Intervenors' calculation also includes an error; the weighted cost of debt should be 3.47%, not 3.37%. The Intervenors' calculation also fails to take into consideration direct costs associated with operating computer systems such as maintenance agreements and personnel costs. As such, the Intervenors' calculation does not produce a representative allocated cost of the billing and accounting systems on a per customer basis.

It is simply too late in this proceeding to conduct the necessary analysis to determine whether the adjustment would lead to just and reasonable rates. Had the Intervenors' presented the allocated costs calculation in testimony, the parties would have had the opportunity to conduct analysis and possibly produce a more representative allocated cost of the billing and accounting systems on the bills paid customers of ACUC and LWUC. Thus, Staff cautions the Commission in accepting the Intervenors' proposal based upon calculations provided in the Intervenors' Initial Brief.

III. OPERATING REVENUES AND EXPENSES

A. Adjustment for Unaccounted-for Water

The Intervenors argue, "[t]he utilities' lack of proper, prudent, and efficient management is further demonstrated by the excessive amount of unaccounted for water (UFW) for both ACUC and LWUC." (ACPOA/LWA IB, p. 26) This theme is reiterated throughout the Intervenors Initial Brief. (See, *Id.*, pp. 3, 23, and 26) While the Company noted (AC Ex. 2.0, p. 19) and Staff agreed (Staff Ex. 6.0, p. 10) that Apple Canyon's

unaccounted for water is greater than expected, and that it is appropriate for Apple Canyon to work toward reducing the amount of unaccounted for water; there is no evidence, or claim by Staff that lack of proper, prudent, and efficient management was a cause, or even a contributing factor, to the problem.

Similarly, Staff's adjustments to operating expenses for unaccounted for water for the two companies were simply based on the requirements of the Companies' tariffs. (Staff Ex. 6.0, p. 10) There is no basis to claim that these adjustments were made based on the Companies' lack of proper, prudent, and efficient management. Neither, is there any support for the Home Owners suggestion that Staff's adjustments for Unaccounted for Water are not large enough. (ACPOA/LWA IB, pp. 3, 27, and 29) There is nothing in the record to support a larger adjustment.

The Home Owners also recommend that the Commission take action against the Companies because of their high levels of unaccounted for water. (*Id.,* pp. 3, 23, and 26) The Commission previously took action when it approved tariffs that limit the amount of cost of unaccounted for water that can be included in rates charged to customers. The record in this docket contains no support for additional action that might be taken by the Commission on this point.

Staff proposed adjustments to decrease maintenance expenses because the unaccounted-for water percentage exceeded the maximum as defined by the Companies' tariffs. (Staff IB, pp. 4-5) The adjustments limit the costs ratepayers bear for unaccounted-for water to what the Commission has set forth as reasonable in each Company's tariffs. These adjustments appropriately address the excess unaccounted for water and the Companies did not contest them. (*Id.*)

B. Test Year O&M and General Expenses

The Companies appear to misunderstand Staff's adjustment to test year O&M and General Expenses. They state that they disagree with "Staff's approach to selectively review and reduce the expense for one account simply because the test year expense for that account may be higher than spending in previous years." (Co. IB, p. 3) Staff did not selectively review and reduce the expense for one account; Staff's adjustment encompasses all expenses except depreciation, taxes, and amortization of CIAC. Further, Staff's adjustment considers expenses in total over a period of years, which belies the Companies' opinion that "Staff's approach fails to recognize that costs associated with a utility's recurring business activities can impact any particular account differently from year to year." (*Id*., pp. 3-4)

Staff disagrees with the Companies' position that historical expenses are much less relevant than current expenses and expenses going forward. (*Id*., p. 4) When expenses fluctuate dramatically from year to year, historical amounts provide a basis for determining a normal level of expenses on which to base rates. Test year expenses for Apple Canyon are 139.5% greater than 2007 expenses and more than double the expenses incurred in previous years. Although test year expense increases for Lake Wildwood are not of the magnitude experienced by Apple Canyon, the increase ranges from 42% over 2007 expenses to 137% over 2004 expenses. (Staff Ex. 2.0, p. 8) By including 2008 with its large increase in the 5-year average, Staff's approach still takes into account the fact that costs do tend to increase over time.

The Companies criticize Staff's adjustment because it is not "known and measurable." (Co. IB, pp. 4-5) The criticism is misplaced as it is the general practice of

the Commission to allow some adjustments other than "known and measurable" adjustments in a historical test year; the Commission routinely allows regulatory adjustments and normalization adjustments. Regulatory adjustments reflect Illinois regulatory policy as demonstrated in the Illinois Public Utilities Act (the "Act"), the Commission's rules found in 83 Illinois Administrative Code, prior Commission orders, and Commission practice. Examples of regulatory adjustments include the removal of promotional advertising and political and lobbying expenses. Rate case expense, which is never completely "known and measurable" until the rate case is completed, also falls into this category as being a regulatory adjustment. Normalization adjustments smooth the impact of unusual levels of revenues or expense. They essentially re-state specific test year data to reflect normal conditions. Examples include adjustments for weather normalization, storm damage, tree trimming, and uncollectibles expense. Staff's adjustment falls into this normalization category. It restates 2008 expenses to a normalized level of expenses and presents a more just and reasonable level of expense that will be in effect during the period that rates are in effect.

The Company argues for the use of 2009 data for O&M expenses. (Id., p. 6) Staff did evaluate the 2009 data. Staff found that Utilities, Inc. began to downsize its staff and consolidate positions in 2009 due to the lack of necessity in direct relation to the amount of capital improvements that are planned for future years. (Staff IB, pp. 8-9) The number of employees decreased from approximately 501 at the end of the test year to 436 at the end of 2009. (*Id*.) For these reasons, Staff believes the normalization adjustment proposed by Ms. Jones, which considers the results from multiple years including the increases in the 2008 test year, presents a more just and reasonable level of expense on which to calculate rates.

C. Corporate Employee Expenses

Staff disagrees with the assessment by the Intervenors that Staff's adjustment to corporate employee expenses is wrong (LWA/ACLPOA IB, p. 26) for two reasons. First, the adjustment was necessary because the corporate employee expenses reflected in the filings for ACUC and LWUC were calculated with incorrect allocation factors. Staff's adjustment applies the correct allocation factors to the total amount to be distributed to all of UI's companies to calculate Apple Canyon's and Lake Wildwood's respective portions. (Staff Ex. 8.0C, p. 14) Second, the salaries of the employees that LWA and ACLPOA appear to take exception to – Steven Winter, Jon Schoenard, Paul Burrus, Thomas Tapella, and L. Goldsmith (LWA/ACLPOA IB, pp. 24-25) – are not included in corporate employee expenses. They are included in operations employee expenses. Disallowance of Staff's adjustment to corporate employee expenses would not affect the amount of expenses allocated to the Companies for these particular employees.

Staff's adjustment to corporate employee expenses is valid and should be adopted by the Commission.

IV. RATE DESIGN/TARIFF TERMS

The proposed tariff sheets the Companies submitted as Exhibit A to its Initial Brief reflect the rate design that has been agreed upon by Staff witnesses Boggs and Rukosuev and the Companies. Staff notes, however, the rates reflected on Exhibit A conform to the revenue requirements the companies are advocating. Thus, the rates are not agreed upon. Staff witnesses Boggs and Rukosuev proposed rates in their direct and rebuttal testimonies based upon Staff's proposed revenue requirements.

In addition, the tariff sheets submitted as Exhibit A reflect a $25 fee for the New Customer Charge. The Companies' current tariffs reflect a $15 New Customer Charge and the Companies did not propose a change to the New Customer Charge in its filing or testimony. Therefore, the Companies tariffs should continue to reflect a $15 New Customer Charge.

V. CONCLUSION

WHEREFORE, for all of the following reasons, Staff respectfully requests that the Commission's order in this proceeding reflect all of Staff's recommendations regarding the Company's request for a general increase in water rates.

June 25, 2010

Respectfully submitted,

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VERIFICATION

I, Mike Ostrander, being first duly sworn, depose and state that I am an Accountant with the Accounting Department of the Financial Analysis Division of the Illinois Commerce Commission; that I have personal knowledge of information stated in the foregoing Reply Brief of the Staff of the Illinois Commerce Commission; and that such information is true and correct to the best of my knowledge, information and belief.

Mike Ostrander

Mike Ostrander
Illinois Commerce Commission

Subscribed and sworn to before me
this 25th day of June, 2010.

Notary Public

OFFICIAL SEAL
LISA BOWMAN
NOTARY PUBLIC, STATE OF ILLINOIS
MY COMMISSION EXPIRES 12-9-2011